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November 18, 1993

HAND DELIVERY

N. Bradley Litchfield, Esq.  
Associate General Counsel  
Federal Election Commission  
999 E Street, N.W.  
Washington, D.C. 20463

Re: Advisory Opinion Request

ADR 1993-23

Dear Mr. Litchfield:

We are counsel to Pacific Telesis Group ("PTG") and, jointly with Kristina Veaco, Senior Counsel of PTG, I am requesting a formal advisory opinion from the Commission as to the applicability of the affiliation rules contained in 11 C.F.R. § 100.5 and § 110.3 to the Pacific Telesis Group Political Action Committee ("PTGPAC") and a new political action committee ("PAC") established recently by PacTel Corporation ("PacTel"), a wholly owned subsidiary of PTG.

PTG, a publicly-held company engaged in the telecommunications business, was formed in 1984 following a consent decree settling antitrust litigation against the American Telegraph and Telephone Company ("AT&T"). The consent decree, known as the Modification of Final Judgment, or "MFJ", required AT&T to divest its regional telephone companies (including Pacific Bell and Nevada Bell, which are now wholly owned subsidiaries of PTG). The MFJ was approved by the United States District Court. United States v. AT&T, 552 F. Supp. 131 (D.D.C. 1982), aff'd sub. nom. Maryland v. United States, 460 U.S. 1001 (1983). The MFJ prohibits the regional telephone companies and their affiliates from providing voice and data services beyond specified geographic boundaries and restricts the lines of business in which the such companies could engage. For example, such companies may not design, develop or manufacture telecommunications equipment or cellular telephones.

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PacTel, which was also formed in 1984, is a holding company engaged in the wireless communications business through various subsidiaries and joint ventures. It is PTG's intention to separate PacTel and create an independent publicly-held company. PTG has proposed the separation for the following reasons: (1) to free PacTel from the MFJ, to which it is currently subject as an affiliate of PTG; (2) to make it easier for the separate companies to obtain financing; and (3) to improve the conditions under which PTG and PacTel and their affiliates operate as a result of their common ownership -- in particular, the affiliate transaction rules imposed by the California Public Utilities Commission.

The first step in the separation of PacTel from PTG will be an initial public offering ("IPO") of 12-14% of PacTel's common stock, which is expected to be completed in early December. On August 27, 1993, PacTel filed a registration statement on Form S-1 (the "S-1") with the Securities and Exchange Commission registering the shares to be sold in the IPO. The remaining 86-88% of PacTel's common stock will continue to be held by PTG. Within six months following the IPO, PTG will distribute the remaining PacTel stock to its shareholders on a pro rata basis (the "Spin-off"). PTG has received a ruling from the Internal Revenue Service to the effect that the Spin-off will qualify as a tax-free distribution under section 355 of the Internal Revenue Code.

In preparation for the IPO and Spin-off, PacTel amended its articles of incorporation and by-laws on October 15, 1993 and September 23, 1993, respectively. The S-1 states that certain provisions of PacTel's articles and by-laws may have the effect of discouraging a tender offer or other takeover attempt. These provisions include: a board of directors with staggered terms; prohibitions against shareholder actions by written consent; and a supermajority (66-2/3%) requirement for amendments to the articles and by-laws. PacTel has also adopted a shareholder rights plan, which may discourage unsolicited takeover attempts.

On April 26, 1993, PTG, as PacTel's principal shareholder, elected three directors, all of whom are also directors of PTG. At PacTel's first annual meeting of shareholders, which will take place within two months after the IPO, nine directors (including the three PTG directors) will be elected, five of whom will serve during the period between the date of the annual meeting and the date of the Spin-off (the "Distribution Date"). The remaining four directors will begin their terms on the Distribution Date. At least four and probably five of the nine directors will have had no previous employment or director

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relationship with PTG. At the time of the Spin-off, the PacTel board members who are also directors or officers of PTG will resign from their PTG positions.

After the IPO, the relationship between PacTel and PTG will be governed by the Separation Agreement, a copy of which is filed as Exhibit 10.1 to the S-1. See p. 80 of the S-1. The Separation Agreement provides that the separation of ownership of PTG and PacTel will be "total and complete" as of the Distribution Date and sets forth the terms pursuant to which the companies will operate during the period between the IPO and the Spin-off as well as after the Spin-off. The clear purpose of this agreement is to divide the assets and liabilities of the companies, and to provide for the separate management of PTG and PacTel. For example, the Separation Agreement provides that between the IPO and the Spin-off, PTG will be able to determine its future business opportunities, even if such determination excludes PacTel from business opportunities that would be considered logical or beneficial to PacTel; provided, however, that PacTel will have an exclusive right to pursue cellular, paging and radio location opportunities.<sup>1</sup> The agreement also provides that PacTel will use its best efforts to continue PTG's insurance policies between the IPO and the Spin-off. The Separation Agreement further provides which agreements between PTG and PacTel will be terminated on the Distribution Date. For example, contracts for general administrative services will be terminated,<sup>2</sup> but contracts for leases and rights-of-way relating to the placement of cellular facilities and agreements for telecommunications services provided under tariff will not be terminated. The Separation Agreement also contains provisions relating to the allocation of intellectual property as of the Distribution Date, the allocation of employee benefit plan assets as of the Distribution Date and the assignment of assets and liabilities.

Immediately after the Spin-off, shareholders of PTG will own approximately 86-88% of PacTel's outstanding common stock. This level of ownership can be expected to change, however, as a

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<sup>1</sup> The allocation of business opportunities provision terminates on the Distribution Date.

<sup>2</sup> PTG will continue to provide administrative services to PacTel through the Distribution Date and that PacTel will compensate PTG for such services. See Appendix F to the Separation Agreement. It is expected that PacTel will provide its own administrative services after the Spin-off.

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result of secondary market trading of the stock of both PTG and Pactel. The persons who are or will be officers and directors of Pactel collectively owned (either beneficially or through presently exercisable stock options) less than 1% of PTG's outstanding stock at September 30, 1993.<sup>3</sup> On the Distribution Date, the options will convert to options to purchase Pactel stock. See p. 70 of the S-1. We do not know what percentage of Pactel's stock that the officers and directors of Pactel will own, although we can assume that they will not, individually or collectively, own a controlling interest. Certain employee benefit plans sponsored by PTG will own stock in both entities, but the total amount of Pactel stock owned by such plans will not exceed 33.2 million shares,<sup>4</sup> or 6.9% of the Pactel stock outstanding on the Distribution Date.<sup>5</sup> Other than the benefit plans, the largest block of PTG stock (less than 3%) is owned by an outside institutional investor.

At the time of the Spin-off, certain employees of PTG will become employees of Pactel, and certain employees of Pactel may become employees of PTG. In no event will any person be employed by both PTG and Pactel, nor will any person be a director of both PTG and Pactel after the Spin-off.

The foregoing is set forth in greater detail in the enclosed Amendment No. 1 to the S-1, including exhibits, which was filed by Pactel with the Securities and Exchange Commission on November 5, 1993.

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<sup>3</sup> At such date, the officers and directors owned 37,204 shares of PTG stock and had exercisable options to purchase another 440,830 shares.

<sup>4</sup> This does not include approximately 8 million shares of stock which have not been allocated under PTG's leveraged employee stock ownership plan. Only the plan trustee, which is independent of PTG management and is subject to the fiduciary provisions of the Employee Retirement Income Security Act of 1974, has the power to vote this stock.

<sup>5</sup> This assumes that there will be approximately 484 million shares of PTG stock outstanding on the Distribution Date; however, this number may increase to approximately 492.5 million, if the underwriters exercise their overallotment options in full.

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PTG sponsors PTGPAC, a "separate segregated fund" which is registered with the Commission and which files reports pursuant to the Federal Election Campaign Act of 1971, as amended, and the regulations and opinions promulgated thereunder by the Commission (hereinafter collectively referred to as the "Act"). After the distribution date, PTG will continue to maintain and sponsor PTGPAC. In anticipation of the Spin-off, Pactel established a PAC ("PACTELPAC") on November 2, 1993. One of the reasons for doing so was to assure continuing employees of PTG and employees of the soon-to-be independent Pactel that their current contributions will not be used to further the political program of a corporation with which they will have no affiliation.<sup>6</sup>

PACTELPAC is currently treated by Pactel as a political committee affiliated with PTGPAC; that is, the two PACs are treated, for the purpose of the Act's contribution limitations, as if they were one PAC. No transfers of funds have been or will be made between the two PACs. After the Spin-off, it is the intention of both PTG and Pactel to treat their respective PACs as unaffiliated and separate because the two committees will no longer be established, financed, maintained or controlled by a single corporation and/or subsidiaries within the meaning of 11 C.F.R. §§ 100.5(g)(2) and 110.3(a)(1)(ii).

We note that in both 11 C.F.R. §§ 100.5(g)(4) and 110.3(a)(3), the Commission has listed "circumstantial factors" which it will consider "in the context of the overall relationship between committees or sponsoring organizations" for the purpose of determining whether or not PACs are affiliated with each other. Although these factors are not conclusive, we understand that the Commission regards them as helpful in determining whether, in a global sense, affiliation exists.

We conclude that only three of the affiliation criteria listed in 11 C.F.R. §§ 100.5(g)(4) and 110.3(a)(3) raise issues germane to the facts specified above.<sup>7</sup>

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<sup>6</sup> Currently, no other affiliate or subsidiary of PTG sponsors a PAC.

<sup>7</sup> The other affiliation criteria are not applicable because: under the Pactel's articles and by-Laws, PTG will not be able to direct or participate in the governance of Pactel (11 C.F.R. §§ 100.5(g)(4)(ii)(B), 110.3(a)(3)(ii)(B)); PTG will not be able to hire or otherwise control the officers or employees of Pactel (continued...)

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11 C.F.R. §§ 100.5(g)(4)(ii)(A) and 110.3(a)(3)(ii)(A) provide that affiliation may be implied if a sponsoring organization owns a controlling interest in the voting stock or securities of the sponsoring organization of another committee. We conclude that since PTG will distribute its shares of PacTel stock to its shareholders in the Spin-off, this criterion will not be met.

11 C.F.R. §§ 100.5(g)(4)(ii)(F) and 110.3(a)(3)(ii)(F) provide that affiliation may be found if a sponsoring organization has members, officers or employees who were members, officers or employees of another sponsoring organization which indicates a "formal or ongoing relationship" between the sponsoring organizations or which indicates the creation of a successor entity. Because some of the employees employed by PacTel as of the Distribution Date will be former employees of PTG (and potentially vice versa), and because PTG could be deemed to have "created" the newly spun-off PacTel, this criterion could be met. However, since the express intention of the Spin-off is to create an entirely independent and competitive new publicly-held corporation and not to launch a vehicle subservient to PTG, there will, in fact, be no formal or ongoing relationship between PTG and PacTel (other than the applicable provisions of the Separation Agreement.)

Finally, we note that 11 C.F.R. §§ 100.5(g)(4)(ii)(I) and 110.3(a)(3)(ii)(I) state that affiliation may be implied when a sponsoring organization or committee had an active or a significant role in the formation of another sponsoring organization or committee. Although PTG formed PacTel, it has proposed to separate that corporation, the purpose of which is to sever, not cement, the relationship between PTG and PacTel and their respective PACs.

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7(...continued)

(11 C.F.R. §§ 100.5(g)(4)(ii)(C), 110.3(a)(3)(ii)(C)); PTG and PacTel will not share any employees, officers or directors (11 C.F.R. §§ 100.5(g)(4)(ii)(E), 110.3(a)(3)(ii)(E)); there has not been and will not be any transfer of funds between PTGPAC and PACTELPAC (11 C.F.R. §§ 100.5(g)(4)(ii)(G) and (H), 110.3(a)(3)(ii)(G) and (H)); and, finally, we do not anticipate that the PTG and PacTel PACs will have patterns of contributions that are any more similar than those of PACs sponsored by similarly situated corporations. (11 C.F.R. §§ 100.5(g)(4)(ii)(J), 110.3(a)(3)(ii)(J)).

In addition to the foregoing circumstantial factors, the Commission has addressed the continuing affiliation of PACs following a tax-free distribution in Advisory Opinions 1986-42 and 1987-21. In both Advisory Opinions, a parent corporation spun off a subsidiary in a tax-free reorganization pursuant to section 355 of the Internal Revenue Code. In each opinion, the Commission relied on a combination of the following factors in concluding that the PACs sponsored by the post-spin corporations were affiliated:

(a) Formation of the subsidiary corporation. In both of the Advisory Opinions, the "parent" formed a new subsidiary corporation in order to transfer a segment of its business into a separate corporation. Pactel is an existing subsidiary of PTG and has been operating as such for nine years. It was not newly formed expressly for the Spin-off. Instead, the Spin-off was proposed for valid business reasons to enable Pactel and PTG to operate independently of one another.

(b) Continuity of shareholder identity. In both of the Advisory Opinions, immediately following the spin-offs, the shareholders of the parent and the newly formed corporation were identical. After the proposed Spin-off of Pactel, the shareholders will not be identical because the IPO will have taken place earlier, resulting in a new group of shareholders that is unlikely to be identical to the PTG shareholders who will receive Pactel stock in the Spin-off. Although PTG's Pactel stock will be distributed to PTG shareholders on the Distribution Date, the stock will be actively traded and, in the normal course, many shareholders will sell their PTG or Pactel stock, and some will sell both stocks.

(c) Board of Directors. In both Advisory Opinions, the parent elected the board of the subsidiary before the spin-off. In Advisory Opinion 1986-42, the parent chose seven of its directors to be on the newly formed subsidiary's 12-member board of directors, thus giving the parent's directors majority control of the subsidiary's board. In Advisory Opinion 1987-21, the parent elected the entire board of the newly formed subsidiary, and four of the nine members of the subsidiary's board also served on the parent's board. Here, before the IPO, Pactel had three directors serving on its board, all of whom also

served on the PTG board. After the IPO and before the Spin-off, PacTel will have its first annual shareholders' meeting where it will elect nine directors, some of whom may also be PTG directors or officers. After the Spin-off, PacTel will have nine directors, at least four and probably five of whom will have no current or past relationship with PTG.<sup>8</sup> The remaining four will have had some prior relationship with PTG, but all four will resign as PTG directors or officers on the Distribution Date. In other words, after the Spin-off, none of PacTel's directors will be directors or officers of PTG.

(d) Overlapping personnel. In both Advisory Opinions, the Commission noted that there was a significant overlap in the personnel and organizational structures between the parent and the spun corporation. As mentioned above, PTG and PacTel will share neither employees, officers nor directors after the Distribution Date. In addition, the Separation Agreement provides that the two companies will operate separately after the Distribution Date.

(e) Articles and by-laws. In both Advisory Opinions, the Commission concluded that the articles of incorporation and by-laws were drafted to perpetuate the parent's control over the spun subsidiary and to make it more difficult for new shareholders to acquire control of the subsidiary. For example, the directors' terms were staggered, the board had authorization to increase the number of directors, supermajority shareholder approval was required for certain corporate reorganizations, shareholders had limited rights to remove directors, and vacancies on the board could be filled by the board. Although the PacTel articles and by-laws contain similar provisions, these are standard anti-takeover provisions. See 1 Fleischer, Takeover Defense 429-436 (4th ed. 1990). In this case, the provisions have been added to protect PacTel from hostile takeovers, not to ensure its continued control by PTG. This is further supported by the fact that PacTel has also adopted a shareholder rights plan or "poison pill."

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<sup>8</sup> The ninth director has not yet been named.

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(f) "Continuity of interest." In Advisory Opinion 1987-21, shareholders of the parent were required to have a "substantial continuity of interest" in the subsidiary after the distribution date. Specifically, this continuity of interest would be satisfied, unless pursuant to a pre-distribution date plan or intent, the parent's shareholders were to sell or otherwise dispose of more than 50% of either the parent's or the subsidiary's stock. PTG has made similar assertions in its Internal Revenue Service Ruling Request. This continuity of interest is required by Internal Revenue Service regulations. See IRS Reg. § 1.355-2(c).

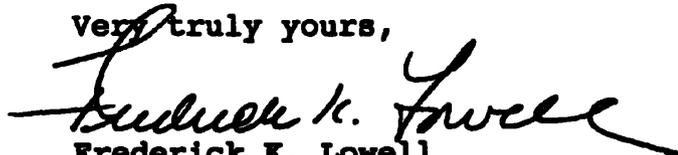
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In light of the foregoing, we would appreciate an opinion from the Commission on the following questions:

1. Under the facts as described above, may PTGPAC and PACTELPAC be treated as disaffiliated as of the Distribution Date?
2. Once disaffiliated, will PACTELPAC be treated as a multicandidate committee pursuant to 11 C.F.R. § 100.5(e)(3)? See Advisory Opinion 1980-40.
3. Assuming that PTGPAC and PACTELPAC cease to be affiliated on the Distribution Date, may each disregard the other's pre-Distribution Date contributions for purposes of complying with the Act's contribution limitations? See Advisory Opinion 1989-16.

We appreciate your attention to this matter and look forward to receiving the Commission's response.

Very truly yours,

  
Frederick K. Lowell

Enc.

Note: OAC will review 300+ page enclosures and circulate pertinent excerpts at a later date as AOR supplement.